SUPREME COURT, U. S.

NO. [redacted] 194

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In the Supreme Court of the United States

OCTOBER TERM, [redacted] 1970

ROBERT W. MONDAY and JOHN A. MONDAY,
Petitioners,

vs.

UNITED STATES OF AMERICA,
Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

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NO.

ROBERT W. MONDAY and JOHN A. MONDAY,
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UNITED STATES OF AMERICA,
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PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

Robert W. Monday and John A. Monday pray that a writ of certiorari issue to review the judgment of the United States Court of Appeals for the Seventh Circuit entered in this case on January 29, 1970.

CITATION TO OPINIONS BELOW

The opinion of the District Court, printed in Appendix B, *infra*, is reported in 294 F.Supp. 1384. The opinion of the Court of Appeals, printed in Appendix A, *infra*, is reported in ..... F.2d .....

JURISDICTION

The judgment of the Court of Appeals was entered on January 29, 1970 and is printed in Appendix C, *infra*. Rehearing was denied on March 17, 1970. The jurisdiction of this Court is invoked under 28 U.S.C., §1254(1).

QUESTIONS PRESENTED

1. Whether failure of corporate officers to pay over federal income and social security taxes withheld from the wages of corporate employees is "willful" within the meaning of the 100% penalty provisions of §6672 of the Internal Revenue Code of 1954, 26 U.S.C., §6672, c. 736 68A Stat. 828, if such failure was with reasonable cause.[1]

2. Whether failure of the Court below to allow John A. Monday a new trial with different instruction denies this Petitioner due process of law and right to trial by jury thereby departing from the accepted and usual course of judicial proceedings and calling for an exercise of this Court's power of supervision.

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[1] Although not propounding them as grounds for granting the writ of certiorari, petitioners also wish to preserve the questions (1) whether the Court below erred in refusing to grant petitioner Robert W. Monday leave to move for judgment notwithstanding the verdict or a new trial on the issue of whether he had a duty to collect, account for and pay over withholding taxes, as requested by petitioner under Rule 50 (d), Federal Rules of Civil Procedure, and *Iacurci* v. *Lummers Co.*, 387 U.S. 86 (1967), and (2) whether the Government's counterclaim should have been dismissed for want of proof. *United States* v. *Rindskopf*, 105 U.S. 418 (1882).

STATUTES INVOLVED

The statutory provisions involved are §§ 6671 and 6672 of the Internal Revenue Code of 1954, 26 U.S.C. §§ 6671, 6672; c. 736 68A Stat. 828:

Sec. 6671. RULES FOR APPLICATION OF ASSESSABLE PENALTIES.

(a) PENALTY ASSESSED AS TAX. — The penalties and liabilities provided by this subchapter shall be paid upon notice and demand by the Secretary or his delegate, and shall be assessed and collected in the same manner as taxes. Except as otherwise provided, any reference in this title to "tax" imposed by this title shall be deemed also to refer to the penalties and liabilities provided by this subchapter.

(b) PERSON DEFINED. — The term "person", as used in this subchapter, includes an officer or employee of a corporation, or a member or employee of a partnership, who as such officer, employee, or member is under a duty to perform the act in respect of which the violation occurs.

Sec. 6672. FAILURE TO COLLECT AND PAY OVER TAX, OR ATTEMPT TO EVADE OR DEFEAT TAX.

Any person required to collect, truthfully account for, and pay over any tax imposed by this title who willfully fails to collect such tax, or truthfully account for and pay over such tax, or willfully attempts in any manner to evade or defeat any such tax or the payment thereof, shall, in addition to other penalties provided by law, be liable to a penalty equal to the total amount of the tax evaded, or not collected, or not accounted for and paid over. No penalty shall be imposed under § 6653 for any offense to which this section is applicable.

CONSTITUTIONAL PROVISIONS INVOLVED

Amendments to the Constitution:

Amendment 5

> No person shall be . . . deprived of . . . property, without due process of law.

Amendment 7

> In suits at common law, where the value in controversy shall exceed twenty dollars, the right of trial by jury shall be preserved, and no fact tried by a jury, shall be otherwise reexamined in any Court of the United States, than according to the rules of the common law.

STATEMENT OF THE CASE

This action arose from a penalty assessed under § 6672 of the Internal Revenue Code of 1954 against Robert Monday for nonpayment of withheld income and social security taxes for the third and fourth quarters of 1960 by the P. C. Monday Tea Company, a Wisconsin corporation of which he was president. Robert Monday made a partial payment of the penalty and brought this action for refund. The jurisdiction of the District Court was invoked pursuant to 28 U.S.C., §§ 1340 and 1346(a), c. 646 62 Stat. 932, 933, because the action arises under the Internal Revenue Code of 1954 and is for the recovery of a tax penalty alleged to have been erroneously assessed and collected. The Government counterclaimed for the unpaid balance of the penalty and impleaded John Monday, vice president-secretary of the corporation, against whom a like penalty had been assessed for the same withheld taxes.

The Mondays were stockholders and directors of the company, which was in the business of selling groceries to housewives through door-to-door truck route salesmen.

There was a distinct division of duties and authority between the Mondays in the actual management of the corporation.

John Monday was the office manager and was in exclusive charge of the company's accounting, pay roll and tax matters (II-Ap. R. 316, 423-5)[2]. He prepared and signed all tax returns, including the quarterly withholding returns here involved (II-Ap. R. 424-5, 442-3).

Robert Monday was exclusively in charge of purchasing from the company's fifty or more suppliers and sales promotion (I-Ap. R. 186-7). At no time did he have or exercise any authority with respect to corporate tax matters since this authority was vested in the company's bookkeeping department, headed by John Monday (I-Ap. R. 195-6, 266; II-Ap. R. 290, 372, 424-5). Robert Monday never prepared, signed or filed any corporate tax return and never had anything to do with payroll accounts (I-Ap. R. 189-90). His corporate duties never included collecting, accounting for or paying over withholding taxes of any type (I-Ap. R. 117, 120-1, 126-7, 130-1, 158, 190, 266; II-Ap. R. 290, 424).

In October, 1960 an independent certified public accountant was retained to analyze the financial condition of the company. Subpoenaed by the Government, the accountant testified that due to incorrect accounting procedures, the company's books overstated assets by nearly a quarter of a million dollars and was in perilous and chaotic financial

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[2] Pursuant to stipulation and permission of the Clerk of this Court, a certified copy of the two volume appendix-record filed in the Court below has been filed here in lieu of the trial transcript. This and similar references are to the volume and page of that appendix-record.

condition (I-Ap. R. 262, 264-5). He disclosed these findings to the Mondays the day before Thanksgiving, 1960 (I-Ap. R. 265). The accountant further testified that throughout his association with the company, which lasted into the spring of 1961, its total working capital never exceeded approximately $185 and that the company was not financially able to make withholding tax payments during this entire period (I-Ap. R. 272; II-Ap. R. 275-6, 280-1, 308). He also testified that the company's expenditures during this period were almost exclusively to acquire stock-in-trade on a C.O.D. basis (I-Ap. R. 230) pursuant to express authorization given by an IRS collection department supervisor, Edward B. Pietrzak, at a conference initiated by the accountant and John Monday.

The Pietrzak conference took place about November 30, 1960 when the accountant and John Monday went to the Milwaukee IRS office and made a complete disclosure of the corporation's financial status and expenditures to Pietrzak. At this time Pietrzak expressly authorized the company to continue operating as it had been and instructed the company to keep current thereafter. Pietrzak specifically authorized continued C.O.D. payments to suppliers. There is no evidence of any payments by the company during or after the quarters in question that exceeded the scope of Pietrzak's authorization. (II-Ap. R. 278-9, 314, 430-34, 436-39).

Because of the continuing expenditures authorized by Pietrzak the company was not able to make the 3rd and 4th quarter 1960 withholding tax payments which totalled about $12,000. Pietrzak then requested a second conference, held in March 1961, well after the close of the quarters in question. This conference was attended by the

accountant, Robert Monday and John Monday. Pietrzak demanded immediate payment of $4,500 for delinquent withholding taxes (I-Ap. R. 192). This was the first time Robert Monday, theretofore concerned solely with his relations with suppliers and with sales efforts, had any knowledge of any withholding tax arrearage on the part of the company (I-Ap. R. 190, 195). Robert Monday thereupon personally borrowed the $4,500 from relatives and paid it to the Government (I-Ap. R. 192-4). Robert Monday believed this payment satisfied all withholding arrearages and made the company current (I-Ap. R. 195).

The company went into receivership in May, 1961 and was adjudicated bankrupt on July 18, 1961.

At the close of the trial the District Court instructed the jury as follows (II-Ap. R. 528):

> "You are instructed that for the Plaintiff's and/or the Third-Party Defendant's failure to pay over the taxes withheld to have been willful, it's not necessary that there have been present any intent to defraud or to deprive the United States of taxes. Nor is it necessary that bad motives or wicked design be shown. The term willful means a voluntary, conscious, and intentional act *done without reasonable cause* to prefer other creditors of the corporation over the Government.
>
> "Mere negligence, that is failure to exercise ordinary care in respect to collecting, truthfully, accounting for or paying over the taxes is not enough to establish willfulness.
>
> "A willful act may also be described as one done intentionally, knowingly and purposefully *without justifiable excuse* as distinguished from an act done carelessly, thoughtlessly, heedlessly or inadvertently.

> A willful act differs essentially from a negligent act. The former, that is willful, is positive; and the latter, that is negligence, is negative." (Emphasis supplied).

The jury's special verdict found both Mondays were under a duty to collect and pay over the taxes in question but that their failure to do so was not willful. Judgment was entered on the verdict in favor of the Mondays following denial of the Government's alternative motions for judgment notwithstanding the verdict or a new trial.

The Court of Appeals reversed and remanded with instructions to enter judgment against John Monday and to grant Robert Monday a new trial on the issue of his willfulness. The Court held reversal was required because the jury instruction on willfulness erroneously included the phrases "without reasonable cause" and "without justifiable excuse." The Court also held that John Monday was not entitled to a new trial by a jury properly instructed on willfulness, that conflicting evidence regarding Robert Monday's lack of knowledge of the withholding tax arrearages entitled him to a new trial, that IRS supervisor Pietrzak's permission to make the expenditures which resulted in the penalties here was irrelevant because it went to the question of reasonable cause and that Pietrzak's permission raised no estoppel against assertion of the penalties because the permission did not include not paying the taxes.

REASONS FOR GRANTING THE WRIT

1. The decision of the Court below is in direct conflict with the decision of the Fifth Circuit Court of Appeals in *Frazier* v. *United States*, 304 F.2d 518 (1962).

In the case at bar the Court below held with respect to the meaning of willfulness in § 6672, Internal Revenue Code of 1954 (Ap. 8, 9 *infra*):

> "The standard of willfulness should not be construed to include lack of 'reasonable cause' or 'justifiable excuse.' * * *
>
> "We therefore hold that the instruction on 'reasonable cause' and 'justifiable excuse' was an impermissible addition to the jury's instruction."

Frazier v. *United States*, also a § 6672 case, held (304 F.2d at 530):

> "We are of the opinion that 'without reasonable cause' as used in the Grandquist and Kellems cases is part of the civil test in determining whether the failure to pay was willful."

The first case referred to by the *Frazier* Court is *Gray Line Co.* v. *Granquist*, 237 F.2d 390 (C.A. 9, 1956), which held that reliance on the advice of an attorney was reasonable cause for failure to pay over a transportation tax collected by the plaintiff bus company from its passengers.[3] Also referred to is *Kellems* v. *United States*,

[3] The subsequent Ninth Circuit case of *Bloom* v. *United States*, 272 F.2d 215 (1959), cert. den. 363 U.S. 803, one of the principal cases relied upon by the Court below, held only (at 223-4) that "without reasonable cause" when included as part of the definition of willfulness in its criminal sense was not a part of the civil test for willfulness. *Bloom* did not overrule the *Gray Line* case.

97 F.Supp. 681, 682 (D.C. Conn. 1951), which held that "willful" as used in § 2707(a) of the 1939 Code, the predecessor of § 6672 and substantially identical to it, means "without reasonable cause" or "capricious."

The Fifth Circuit reaffirmed its definition of willfulness in *Cash* v. *Campbell*, 346 F.2d 670, 672 (1965), and in *Gefen* v. *United States*, 400 F.2d 476, 482, n.7 (1968), cert. den. 393 U.S. 1119.

The decision of the Court below also conflicts with the definition of willfulness prevailing in the Eighth Circuit, expressed in *United States* v. *Strebler*, 313 F.2d 402, 403, n.2 (1963).

In the Third Circuit the District Court's decision in *United States* v. *Slattery*, 224 F.Supp. 214 (E.D. Pa. 1963), expressly approving (at 218) "reasonable cause" as a defense to the § 6672 penalty for willful nonpayment of withheld taxes, was affirmed *per curiam*. 333 F.2d 844 (C.A. 3, 1964).

The First and Second Circuit Courts of Appeals appear not to have encountered the question directly but District Courts there approved reasonable cause as a defense to willfulness in *Paisner* v. *O'Connell*, 208 F.Supp. 397 (D.C.R.I. 1962), and *Kellems* v. *United States*, 97 F.Supp. 681 (D.C. Conn. 1951).

2. Resolution of the question whether lack of reasonable cause is a component of willfulness is important for consistent administration of § 6672 of the Internal Revenue Code of 1954. The annotation in 22 ALR 3d 8, 82-96, collects many cases involving § 6672 that have expressed a definition of willfulness. The confusion there apparent in the differing interpretations of willfulness by the District

Courts and Courts of Appeals has clearly bred litigation and deprives the Government as well as officers of financially troubled corporations of reliable guidelines.

It was remarked in *Frazier* v. *United States*, 304 F.2d 528, 529:

> "As with many issues, the definition of 'willful' has been smothered with a maze of semantics. The following are some examples of this confusion of words. In the Bloom case itself [Bloom v. United States, 272 F. 2d 215 (C.A. 9, 1959)], the court specifically holds that it is not necessary for application of the civil penalty to prove that the act was done 'without reasonable cause.' At the same time, the Bloom court, in support of its conclusion that only a voluntary, conscious and intentional act need be shown, cites Kellems v. United States, 97 F.Supp. 681 (Conn. 1951), a case which does consider 'without reasonable cause' as part of the civil test. In addition, in an earlier Ninth Circuit case, Gray Line Co. v. Grandquist, 237 F.2d 390, 395 (9 Cir. 1956), the same court held that where the failure to pay was conscious and intentional, but motivated by reasonable cause, the penalty will not lie. The reasonable cause in that case was reliance on the advice of counsel that the taxes were not due. There is no indication in Bloom that the court intended to overrule this precedent. Moreover, this same semantic confusion may be found in cases the appellant relies on."

We believe the *Frazier* Court's comment on the state of the law is accurate and that this Court alone can settle the question.

3. Petitioners believe the decision in the Court below is erroneous and the conflicting decision of the Fifth Circuit Court of Appeals in *Frazier* v. *United States* is correct. The instant case is a prime example of why the door

must be left open, as in *Frazier*, for consideration of special circumstances tending to exculpate corporate officers in appropriate cases. The District Court said in its opinion (Ap. 17-18, *infra*):

> "The Government argues that the action of the supervisor in giving the corporation permission to buy on a cash basis in no way relieved the Mondays of their legal responsibilities and therefore is immaterial. I agree that the action of the supervisor in no way relieved the Mondays of their legal responsibilities, but I believe it was admissible so that the jury could consider this evidence along with the other evidence in determining whether the Monday's action was willful. This is especially so in view of the fact that the essence of the Government's case is that the Mondays bought this merchandise instead of paying the money over to the Government, and that this constituted a preference over the Government."

> "2. Note: This is not a case where a corporation gives a preference to pre-existing creditors. At the most, the Mondays were paying after-acquired creditors (i.e., suppliers) with the permission of the Internal Revenue Service."

The District Court also said (App. 24, *infra*):

> "The situation in which the Mondays found themselves presents even more compelling reasons for concluding that the failure to pay the taxes was not 'willful.' The Mondays continued their business and paid for supplies in reliance upon the specific permission of an officer of the Internal Revenue rather than mere advice of attorneys."

In a similar context Treasury Regulations define reasonable cause as ordinary business care and prudence. Reg. §301.6651-1 (a)(3). Rudimentary justice would seem to require that the 100% penalty, harshest of civil tax penalties

and harsher even than some fraud penalties,[4] not be imposed for conduct expressly authorized by a responsible IRS officer. The Government ought not to be heard to say that reliance on such authorization does not constitute ordinary business care and prudence. The Draconian approach adopted by the Court below sacrifices even the minimal flexibility the opposing *Frazier* rule would and should allow.

Petitioners respectfully disagree with the view of the Court below (App. 8, *infra*), that the defense of reasonable cause necessarily evokes notions of evil motive or bad purpose. This is avoided when a jury instruction, as the one given in this case, quoted at p. 7-8, *supra*, expressly rules out such notions. Evil intent, essential to criminal liability, is indeed irrelevant to civil liability and should properly be ignored in determining whether a course of conduct is objectively reasonable. It is submitted that the Court below mistakenly believed that evil motive and lack of reasonable cause are the same thing.

The issue is whether the courts may evaluate the objective reasonableness of a taxpayer's course of conduct in a civil penalty case without regard to the propriety of his intentions. The decision of the Court below needlessly abjured the power so to do.

4. The failure of the Court below to allow John A. Monday a jury trial constitutes a denial of 5th and 7th Amendment rights. The Court of Appeals arbitrarily found the conduct of John A. Monday to be willful without submitting the issue to the jury.

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[4] Compare, e.g., §6653 (b), I.R.C. 1954: 50% penalty for fraudulent under-payment of income, estate or gift taxes; §6653(e), I.R.C. 1954: 50% penalty for willful failure to pay stamp taxes.

The constitutional right of trial by a properly instructed jury is absolute and cannot be restricted or limited by either Congress or the courts. *Beacon Theatres, Inc.* v. *Westover,* 359 U.S. 500 (1959); *Lyon* v. *Mutual Benefit Health & Acc. Assn.,* 305 U.S. 484 (1939).

The Appellate Court is prevented from entering judgment on the facts, or taking any action equivalent thereto, after a verdict by the jury on the evidence. *Slocum* v. *New York L. Ins. Co.,* 228 U.S. 364 (1913).

The denial of a new trial to John A. Monday is inconsistent with a previous mandate of the Seventh Circuit Court. *Dazenko* v. *James Hunter Machine Co.,* 393 F.2d 287 (C.A. 7, 1968).

John A. Monday should be granted a new trial if the lower court erroneously instructed the jury on a material matter.

The Court below acted in excess of its authority and was without jurisdiction to foreclose John A. Monday from a new trial by jury because of the 5th and 7th Amendments to the Constitution.

Previous decisions of this Court have been ignored and the Seventh Circuit Court of Appeals has so far departed from the accepted and usual course of judicial proceedings as to call for an exercise of this Court's power of supervision.

CONCLUSION

Petitioners pray that a writ of certiorari issue for the foregoing reasons.

Respectfully submitted,

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May 8, 1970

APPENDIX A

Opinion Of The
UNITED STATES COURT OF APPEALS
For The Seventh Circuit

SEPTEMBER TERM, 1969 SEPTEMBER SESSION, 1969

(Caption Omitted)

JANUARY 29, 1970

Before KNOCH, *Senior Circuit Judge,* CUMMINGS, *Circuit Judge,* and STECKLER, *District Judge.*[1]

CUMMINGS, *Circuit Judge.* This case involves the question whether Robert and John Monday are personally liable for the P. C. Monday Tea Company's (the "Company") failure to pay to the Government social security and income taxes withheld from its employees.

The Company was organized in 1918 and sold groceries to housewives through door-to-door truck route salesmen. During the latter half of 1958 and thereafter, Robert Monday was president and John Monday was vice president and secretary of the Company, which had 55 employees. John Monday signed and participated in the preparation of the Company's tax returns.

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[1] William E. Steckler, Chief Judge of the United States District Court, Southern District of Indiana, is sitting by designation.

In 1956, the financial condition of the Company began to deteriorate. By 1960, its annual gross income was half the average of the previous five years. It could acquire merchandise for resale from its suppliers only on a C.O.D. basis. During the third and fourth quarters of 1960, the Company paid wages to its officers and employees and deducted federal income and social security taxes from the wages. It failed, however, to pay the Government the withheld taxes of $6,619.53 on October 31, 1960, and $5,764.48 on January 31, 1961, the respective due dates for the quarterly payments. In November or December 1960, it belatedly filed its return for withheld taxes for the third quarter of 1960 and it also failed to file its return for the fourth quarter of 1960 until March 1961. Nevertheless, during these quarters, the Company continued to pay business creditors for antecedent debts and for merchandise purchased C.O.D.

In March 1961, Robert Monday borrowed $4,500 from his sister in response to the Internal Revenue Service's March 1961 demand for payment of withheld social security and income tax moneys of the Company's employees. John Monday testified that this sum was to cover the withheld taxes for the first quarter of 1961, but Robert Monday testified he thought the payment of $4,500 satisfied all withholding arrearages and made the Company current. In fact, after the $4,500 payment the Coupany was still delinquent as to the last two quarters of 1960.

In May 1961, the Company went into receivership, and it was adjudicated bankrupt in July 1961. In the bankruptcy proceedings, the Government filed claims for various classes of taxes for 1960 and 1961, including the amounts here in issue. These claims were allowed in the

sum of $22,494.53, and in September 1963, the Government realized $10,978.25 on them. Although the bankruptcy referee directed that this amount be applied to the most recent claims of the Government, the Government applied $3,167.57 to the Company's withholding liability for the second quarter of 1960 and only applied $435.84 to the third quarter of 1960, thus leaving unsatisfied most of the Government's claim for the third and fourth quarter 1960 withholding taxes. The bankruptcy referee also assigned to the Government $7,400 of the Company's accounts receivable, but the trial did not disclose whether any of these were collected by the Government.

In March 1964, the Internal Revenue Service assessed a 100% penalty in the amount of $12,384.01[2] against Robert Monday pursuant to Section 6672 of the Internal Revenue Code of 1954.[3] This assessment was based on the Company's failure to pay to the Government the federal income and social security taxes withheld from the wages

[2] In January 1965, this assessment was abated in the amount of $435.84 received from a bankruptcy distribution and applied to the third quarter of 1960.

[3] Section 6672 (26 U.S.C. § 6672) provides:

"Any person required to collect, truthfully account for, and pay over any tax imposed by this title who willfully fails to collect such tax, or truthfully account for and pay over such tax, or willfully attempts in any manner to evade or defeat any such tax or the payment thereof, shall, in addition to other penalties provided by law, be liable to a penalty equal to the total amount of the tax evaded, or not collected, or not accounted for and paid over. No penalty shall be imposed under section 6653 for any offense to which this section is applicable."

of its employees during the third and fourth quarters of 1960. In March 1966, Robert Monday paid $1,112 of this assessment under protest. In May 1966, he filed this suit in the district court seeking to recover that amount plus interest and seeking a declaration that the penalty assessment against him was null and void. The Government counterclaimed for $10,836.17, the balance of the assessment, plus interest. The Government also filed a third-party complaint against John Monday seeking to recover $11,948.17, plus interest, pursuant to a November 1964 assessment aaginst him under Section 6672 of the Internal Revenue Code.

At the close of the trial, the jury found that Robert and John Monday were under a duty to collect and pay the withheld taxes to the Government for the two quarters in question, pursuant to Sections 6671(b) and 6672 of the Internal Revenue Code of 1954, but that they did not willfully fail to pay the taxes. Therefore, judgment was entered for the Mondays. The district court subsequently denied the Government's motion for judgment notwithstanding the verdict or for a new trial (294 F.Supp. 1384) and this appeal followed.

Sufficiency of Evidence to Support Jury's Finding that Robert Monday Had a Duty to Collect and Pay These Taxes to the Government

Under Section 7501 of the Internal Revenue Code, the amount of the withheld income and social security taxes deducted from the Company's employees' wages in the third and fourth quarters of 1960 was "to be a special fund in trust for the United States." See *In the Matter of Halo Metal Products, Inc.* v. *Randall*, ... F.2d ..... (7th Cir. 1969). The "person" liable for withheld taxes under Section 6672 of the Code includes an "officer or

employee of a corporation, * * * who as such officer, * * * is under a duty'' to see that the funds are remitted to the Government. 26 U.S.C. § 6671(b). The jury specially found that both Robert and John Monday had a duty to collect and pay the Government taxes deducted in the third and fourth quarters of 1960. Robert Monday contends that as to him, this finding cannot be sustained. Our examination of the record reveals sufficient support for the special verdict.

Corporate office does not, *per se*, impose the duty to collect, account for and pay over the withheld taxes. On the other hand, an officer may have such a duty even though he is not the disbursing officer. Cf. *Bloom* v. *United States*, 272 F.2d 215 (9th Cir. 1959), certiorari denied, 363 U.S. 803. The existence of the same duty and concomitant liability in another official likewise has no effect on the taxpayer's responsibility. *Datlof* v. *United States*, 252 F.2d 11, 33 (E.D. Pa. 1966), affirmed, 370 F.2d 655 (3d Cir. 1966), certiorari denied, 387 U.S. 906. Liability attaches to those with power and responsibility within the corporate structure for seeing that the taxes withheld from various sources are remitted to the Government. *Scott* v. *United States*, 354 F.2d 292, 296 (Ct. Cl. 1965); see also *Gefen* v. *United States*, 400 F.2d 476, 482 (5th Cir. 1968), certiorari denied, 393 U.S. 1119. This duty is generally found in high corporate officials charged with general control over corporate business affairs who participate in decisions concerning payment of creditors and disbursal of funds. Cf., *e.g.*, *Bloom* v. *United States*, 272 F.2d 215 (9th Cir. 1959), certiorari denied, 363 U.S. 808; *Hewitt* v. *United States*, 377 F.2d 921, 924 (5th Cir. 1967); *Scott* v. *United States*, 354 F.2d 292 (Ct. Cl. 1965); *Newsome* v. *United States*, 301 F.Supp. 757 (S.D. Texas 1968); see generally, 8A *Mertens, Law of Federal Income Taxation*, § 47A.25a, pp. 126-128 (1964).

Under the corporate by-laws, Robert Monday's duties as president included "general supervision of the affairs of the corporation." Through his own stock ownership and through a voting trust, he controlled the Company. He and his brother signed most of the corporate checks, and both of them conferred from time to time as to what creditors should be paid. They sought payment from Robert, not John. Robert Monday had signed corporate checks payable to the Government with respect to prior withholding taxes. In John's absence, Robert performed John's duties. Robert also admitted having read a report prepared by the Company's certified public accountant informing him of the then overdue taxes. Regardless of the purchasing and promotional activities of Robert, there was ample evidence to sustain the jury's conclusion on this point. Cf. *Kelly* v. *Lethert*, 362 F.2d 629, 634 (8th Cir. 1966).

Correctness of Willfulness Instruction

Over the objection of the Government, the district court gave the following instruction as to the meaning of the word "willful" in Section 6672 (note 3 *supra*):

> "You are instructed that for the plaintiff's and/or third-party defendant's failure to pay over the taxes withheld to have been willful it is not necessary that there have been present any intent to defraud or to deprive the United States of taxes, nor is it necessary that bad motives or wicked design be shown.
>
> "The term 'willful' means a voluntary, conscious and intentional act, done *without reasonable cause*, to prefer other creditors of the corporation over the government.

"Mere negligence, that is, failure to exercise ordinary care, in respect to collecting, truthfully accounting for or paying over the taxes is not enough to establish willfulness.

"A 'willful' act may also be described as one done intentionally, knowingly, and purposely, *without justifiable excuse*, as distinguished from an act done carelessly, thoughtlessly, heedlessly, or inaadvertently.

"A 'willful' act differs essentially from a 'negligent' act. The former, that is 'willful,' is positive; and the latter, that is 'negligence,' is negative." (Emphasis supplied.)

The Government asserts that it was improper for the district court to permit the jury to excuse acts done with "reasonable cause" or "justifiable excuse." We agree that it was improper to include these terms in the instruction.[4]

The precise content to be given the concept of "willfulness" varies according to the legal context in which it appears. In criminal stautes, "willfulness" generally requires bad purpose or the absence of any justifiable excuse. *United States* v. *Murdock*, 290 U.S. 389, 394. In civil actions, however, these elements need not be present. Rather, willful conduct denotes intentional, knowing and voluntary acts. It may also indicate a reckless disregard for obvious or known risks.

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[4] In addition, the Government argued that even if some "reasonable cause" instruction were proper, the district court erroneously failed to explain its meaning and thereby permitted the jury to conclude that the financial straits of the corporation constituted such a reasonable cause.

Despite its denomination as a "penalty" assessment, the statutory liability imposed by Section 6672 is essentially civil in nature. *Cash* v. *Campbell*, 346 F.2d 670, 673 (5th Cir. 1965). Its basic purpose is the protection of governmental revenue. *Botta* v. *Scanlon*, 314 F.2d 392, 393 (2d Cir. 1963); *Spivak* v. *United States*, 370 F.2d 612, 616 (2d Cir. 1967), certiorari denied, 387 U.S. 908. It provides a remedy to prevent the unnecessary loss of tax funds by permitting the "tax authority to reach those responsible for the corporation's failure to pay the taxes which are owing." *United States* v. *Graham*, 309 F.2d 210, 212 (9th Cir. 1962); *White* v. *United States*, 372 F.2d 513, 516 (Ct. Cl. 1967). In light of this purpose, we agree with those courts which have defined willful action under Section 6672 as referring to voluntary, conscious and intentional—as opposed to accidental—decisions not to remit funds properly withheld to the Government. *Spivak* v. *United States*, 370 F.2d 612, 615 (2d Cir. 1967), certiorari denied, 387 U.S. 908; *Cross* v. *United States*, 311 F.2d 90, 94 (4th Cir. 1962); *Hewitt* v. *United States*, 377 F.2d 921, 924 (5th Cir. 1967); *Flan* v. *United States*, 326 F.2d 356, 358 (7th Cir. 1964); *Bloom* v. *United States*, 272 F.2d 215, 223 (9th Cir. 1959), certiorari denied, 363 U.S. 803; *Scott* v. *United States*, 354 F.2d 292, 295 (Ct. Cl. 1965). Liability does not depend upon the presence of bad motive or the specific intent to defraud the Government or deprive it of revenue. *White* v. *United States*, 372 F.2d 513, 521 (Ct. Cl. 1967).

The standard of willfulness should not be construed to include lack of "reasonable cause" or "justifiable excuse." These concepts tend to evoke notions of evil motive or bad purpose which properly play no part in the civil definition of willfulness. Cf. *Bloom* v. *United States*, 272 F.2d 215,

223-224 (9th Cir. 1959), certiorari denied, 363 U.S. 803; accord, *Flan* v. *United States*, 326 F.2d 356, 358 (7th Cir. 1964); *White* v. *United States*, 372 F.2d 513 (Ct. Cl. 1967). In addition, "reasonable cause" and "justifiable excuse" invite consideration of such misleading and improper factors as the financial condition of the business or the demands of creditors. Cf. *United States* v. *Hill*, 368 F.2d 617, 621 (5th Cir. 1966); *United States* v. *Strebler*, 313 F.2d 402, 404 (8th Cir. 1963); *Frazier* v. *United States*, 304 F.2d 528, 529-530 (5th Cir. 1962). The defenses countenanced by the district court's use of "reasonable cause" and "justifiable excuse" are inconsistent with the purposes of Congress to protect the sources of revenue by permitting recovery from those individuals charged with the responsibility of transferring withheld funds to the Government.

We therefore hold that the instruction on "reasonable cause" and "justifiable excuse" was an impermissible addition to the jury's instructions. The district court should have adopted the following part of the Government's proffered instruction on wilfulness:

> "You are instructed that for the plaintiff and/or third-party defendant's failure to pay over the taxes withheld to have been willful it is not necessary that there have been present any intent to defraud or to deprive the United States of taxes; nor is it necessary that bad motives or wicked design be shown.
>
> "An act is willful if it is voluntary, conscious, and intentional. If you find that plaintiff and/or third-party defendant knowingly used available funds to prefer other creditors over the United States then you must find that he acted willfully."

Despite the erroneous instruction given, we must still consider whether there is sufficient evidence against John and Robert Monday to require a directed verdict in favor of the Government against either brother rather than a new trial.

Evidence of John Monday's Willfulness

John Monday was the vice president and secretary and a director of the Company. It is uncontested that he was in charge of corporate tax matters. Before their due dates, he and the Company's bookkeeper prepared the quarterly returns in issue, and John Monday signed them as vice president. Each was filed belatedly and without payment although appropriate checks had evidently been prepared. In his testimony, he stated that during the third and fourth quarters of 1960, he knew these withholding taxes were due and owing and nevertheless wrote checks to other creditors and suppliers of the corporation instead of paying the United States out of otherwise available funds. This preference of others over the Government was clearly an intentional act requiring a verdict in favor of the Government against John Monday since a contrary verdict could never stand.

Evidence of Robert Monday's Willfulness

Deane Nichol, the certified public accountant employed by the Company in the fall of 1960, testified that he pointed out to Robert in November 1960 that the Company had not paid taxes withheld from its employees and told him of the possible penalties. Robert admitted that he read Deane Nichol's report which reflected the delinquent taxes. Robert conferred with his brother John as to what creditors should be paid and signed checks covering previous trust tax payments to the Government. Robert knew the Company withheld taxes and was supposed to forward them to the Government. He performed John's functions when John was absent. Since John admitted

the $4,500 March 1961 payment was only for the first quarter of 1961, the jury could disbelieve Robert's statement that he thought it covered the delinquent quarters as well. On the other hand, Robert testified that he did not know of the tax arrearage until March 1961. Because of conflicts in the evidence, there must be a remand with respect to Robert, so that a properly instructed jury can resolve the question of his willfulness.

Meetings with the Internal Revenue Service

The chief defense presented by the Monday brothers revolves around their meetings with Edward Pietrzak, collection department supervisor of the Internal Revenue Service in Milwaukee, Wisconsin. The court below felt that the content of these meetings was relevant to the determination of willfulness. In addition, plaintiff Robert W. Monday contends that as a result of these meetings, the Government is estopped to seek recovery from the Company's officers under Section 6672. We disagree with both propositions.

The evidence of the meetings was directed to the establishment of a "reasonable cause" or "justifiable excuse" for the parties' failure to perform their duties with respect to the withholding taxes.[5] It was intended to negate any inference of bad faith or improper motivation by establishing reasonable reliance upon the representation that the moneys need not be collected and remitted. Since, as seen, the Mondays are foreclosed from relying upon "reasonable cause" or "justifiable excuse" as an element of willfulness under this Section, they may find no solace in the meetings in this respect.

Nor does the testimony of the content of the meetings support any claim that the Government should be estopped

[5] This purpose is clear from the discussion of the matter in the district court's opinion. 294 F.Supp. at 1387, 1389.

because of the statements made by Pietrzak. The first meeting of the Government's agent and the Company's representatives took place on November 30, 1960. Since this meeting occurred one month after the due date for the third quarter taxes, it furnished no excuse for the previous failure to collect and remit the funds. Neither at that time nor at the subsequent meeting in March 1961, did Pietrzak give the Company or its individual officers any indication that they were relieved of their responsibilities under the various Sections of the Code. At the November meeting, moreover, Pietrzak specifically instructed the Company to keep current, thus precluding any claim that its subsequent failure to remit the fourth quarter taxes resulted from reliance upon his authorization of continued business. In any event, the corporate and individual liabilities under Section 6672 are separate and distinct. Cf. *Datlof* v. *United States*, 370 F.2d 655, 656 (3d Cir. 1966), certiorari denied, 387 U.S. 906. The taxpayers have failed to disclose any action by the Government upon which they could reasonably have relied as the grounds for their failure to collect and remit any of the taxes withheld from their employees. Cf. *Spivak* v. *United States*, 370 F.2d 612, 615 (2d Cir. 1967), certiorari denied, 387 U.S. 908.[6]

Bankruptcy Proceedings

Finally, the Mondays argue that the assessments against them are improper because the Internal Revenue Service did not apply the $10,978.24 bankruptcy proceeds to the Government's most recent tax claims, as directed by the

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[6] Because Pietrzak did not forgive the delinquent taxes and insisted that the Company henceforth keep current, there is no need to enter the troubled arena of when the doctrine of estoppel is applicable to the Government. See 2 Davis, *Administrative Law Treatise* §§ 17.01-17.04 (1958); 10 Mertens, *Law of Federal Income Taxation* §§ 60.14, 60.15 (1964).

bankruptcy referee. As the testimony shows, the Internal Revenue Service deliberately ignored the bankruptcy referee's direction and applied these proceeds to earlier periods for the "best benefit of the government," thus preserving the claims against Robert and John Monday individually for the quarters in question under Section 6672.

As previously noted, the personal liability imposed upon the individual taxpayer by Section 6672 is separate and distinct from that imposed upon the employer under Section 3403 of the Code. *Datlof* v. *United States*, 370 F.2d 655, 656 (3d Cir. 1966), certiorari denied, 387 U.S. 906. It is not dependent upon rules governing the liability of the employer. Cf. *Rosenberg* v. *United States*, 327 F.2d 362 (2d Cir. 1964); *Kelly* v. *Lethert*, 362 F. 2d 629 (8th Cir. 1966). In *Spivak* v. *United States*, 370 F.2d 612 (2d Cir. 1967), certiorari denied, 387 U.S. 908, the court rejected a similar contention that the government's compromise of its claim for taxes against a bankrupt corporation which expressly provided that the government would assert no further claim against the corporation for withholding taxes, should bar the subsequent recovery from responsible officers under Section 6672.[7] Here too,

[7] In *Spivak* the compromise of the bankrupt corporation's debt specifically provided that it should not prejudice further proceedings against corporate officers for penalties such as that created by Section 6672. While the referee's order in this case cannot satisfy or remove the officers' liability, it might nevertheless bar action against the Mondays were they to show that an administrative practice existed, such as referred to in *Spivak*, that the Government would not press its claim against the responsible officers where the corporate obligation has been met. Cf. 370 F.2d at 615. Since the parties have not argued this question and there is no evidence at this time of any such administrative practice, we do not express any opinion on this point.

the separate nature of the tax liabilities imposed upon the Mondays precludes their assertion of any satisfaction of the Company's liability for withholding taxes as a satisfaction of their individual liability under Section 6672.[8]

For the foregoing reasons, the judgment of the district court is reversed with instructions to enter judgment for the United States against John A. Monday and to grant a new trial to Robert Monday to determine, upon proper instructions to the jury, the question of his willfulness.

Reversed and remanded.

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[8] For this reason, absent any showing of an administrative practice mentioned in note 7, *supra*, the district court need not consider the question of the propriety of the Commissioner's computations of the amount of taxpayers' liability insofar as the Government may have collected any of the $7,400 of accounts receivable assigned to the Government by the bankruptcy referee.

APPENDIX B

OPINION AND ORDER OF THE DISTRICT COURT ON DEFENDANT'S MOTION FOR JUDGMENT NOTWITHSTANDING THE VERDICT, OR FOR A NEW TRIAL. (Caption omitted.)

INTRODUCTION

This opinion on the Government's motions after verdict is primarily concerned with the proper construction of the word "willfully" as used in § 6672 of the Internal Revenue Code.[1] The Government, in effect, claims that the word "willfully" does not include the concept of reasonable cause and in effect means "knowingly."

This court believes that the word in the statute has a meaning which in part encompasses the concept that where the failure to do the required act is based on reasonable cause, then such failure is not willful. As will be seen later, if this court's interpretation of the word is correct, then the Government's motions after verdict must be denied; and, of course, if this court is in error on the meaning of "willful," then the Government's motions should have been granted.

A penalty assessment under 26 U.S.C. § 6672 was made against Robert W. Monday for the withholding and F.I.

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[1] § 6672 "Failure to collect and pay over tax, or attempt to evade or defeat tax

"Any person required to collect, truthfully account for, and pay over any tax imposed by this title who willfully fails to collect such tax, or truthfully account for and pay over such tax, or willfully attempts in any manner to evade or defeat any such tax or the payment thereof, shall, in addition to other penalties provided by law, be liable to a penalty equal to the total amount of the tax evaded, or not collected or not accounted for and paid over. No penalty shall be imposed under section 6653 for any offense to which this section is applicable."

C.A. taxes withheld from wages of employees of the P. C. Monday Tea Company for the last two quarters of 1960. Partial payment was made under protest, and timely claim for refund was made. The District Director of Internal Revenue denied the claim for refund. Robert W. Monday then instituted this action for recovery of the amount so paid. The Government counterclaimed for $10,836.17, the balance of the assessment, and interpleaded John A. Monday as a third-party defendant, claiming that he was equally liable with Robert W. Monday under the counterclaim.

Trial to a jury was had from June 4, 1968 to June 7, 1968. The jury found that both Robert W. Monday and John A. Monday were *responsible* officers for the periods in question pursuant to § 6672. The jury also found that neither John A. Monday nor Robert W. Monday *willfully* failed to pay the taxes in question. Accordingly, judgment was entered for the Mondays on June 11, 1968. The Government filed motions for judgment notwithstanding the verdict or, in the alternative, for a new trial.

FACTS

The P. C. Monday Tea Company (hereinafter called the "Company") was organized in 1918 by the father of Robert and John Monday. In 1960, the Company, which had about fifty-five employees, sold groceries to housewives, door to door, on a delivery route basis. The salesmen carried the groceries with them in their trucks.

During the last half of 1960 and thereafter, Robert W. Monday was president and a director and John A. Monday was vice president, secretary, and a director of the Company. Both Robert and John Monday were active in the management of the business, although there was a substantial division of authority between them. John A. Mon-

day spent virtually all of his time in the office, and Robert W. Monday was in the office about 25 per cent of the time. John A. Monday signed and participated in the preparation of the corporate tax returns.

The employer's quarterly federal tax returns were timely filed for the period in question without remittance. Both of the Mondays had the authority to sign checks, and together they negotiated loans and signed notes and mortgages as necessary.

In about 1956, the financial condition of the Company took a decided turn for the worse. This condition continued so that by 1960 the annual gross of the Company was only about half of its annual gross of the previous five years.

After 1960, the Company acquired its merchandise virtually on a c.o.d. basis. In March 1961, the Monday brothers went to the Milwaukee Internal Revenue Office to discuss the withholding tax arrearage. Despite the withholding tax arrearage, they were given specific permission by a supervisor in the Collection Department to continue to buy merchandise on a cash basis so that the Company could stay in business.

The Government argues that the action of the supervisor in giving the corporation permission to buy on a cash basis in no way relieved the Mondays of their legal responsibilities and therefore is immaterial. I agree that the action of the supervisor in no way relieved the Mondays of their legal responsibilities, but I believe it was admissible so that the jury could consider this evidence along with the other evidence in determining whether the Mondays' action was willful. This is especially so in view of the fact that the essence of the Government's case is

that the Mondays bought this merchandise instead of paying the money over to the Government, and that this constituted a preference over the Government.[2]

In spite of this cash operation, the Company went into receivership in May of 1961. Bankruptcy followed on July 18, 1961. In September 1963, the trustee in bankruptcy distributed to the District Director the amount of $10,978.24, of which $435.84 was applied to the taxes on which the penalty assessment was based.

As indicated at the outset, all but one of the questions now raised by the Government result from a dispute as to the meaning of the word "willfully" in § 6672 of the Internal Revenue Code. The Government contends that if a responsible officer knew the taxes were due and the corporation had *any* money that was not used to pay the taxes, then the failure to pay was, as a matter of law, willful. In essence, the Government would impose on the responsible officer a form of strict liability for the taxes if there was any money coming into the hands of the corporation and if such officer knew the taxes were due and owing.

The statute in question, however, uses the word "willfully" not once but twice. Had that word been omitted, the type of liability suggested by the Government would exist. If Congress had wanted to hold the responsible officer strictly liable for the taxes if there was at any time any money available in the corporation, it could have done so with direct language by making such officer personally liable. The Government here is trying to impose such a

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[2] Note: This is not a case where a corporation gives a preference to pre-existing creditors. At the most, the Mondays were paying after-acquired creditors (i.e., suppliers) with the permission of the Internal Revenue Service.

standard of strict liability on the responsible officer. I do not believe that to be the law. Congress said that for a person to be liable for the tax, he must be a responsible officer who "*willfully* fails to * * * pay over such tax * * *." Consequently, an intentional failure which cannot be negated by a reasonable cause on the part of the responsible officer is essential to a finding of liability. To hold otherwise would render nugatory the very language of the statute. This court respectfully declines to rewrite the statute as the Government now requests.

IS THERE EVIDENCE WHICH SUPPORTS THE JURY FINDING THAT THE MONDAYS DID NOT WILLFULLY FAIL TO PAY THE TAXES IN QUESTION?

The Government has moved for judgment notwithstanding the verdict. If it can be said that no evidence supports the finding of the jury, the Government must prevail. In the view of this court, however, there is evidence from which the jury could infer that the failure by Robert and John Monday to pay over the taxes in question was not a willful failure as "willfully" was defined in the instructions given by this court, which will be discussed later.

The jury could find that the specific permission given by the supervisor in the Collection Department of the Milwaukee Internal Revenue Office to buy merchandise on a cash basis, despite the withholding tax arrearage, constituted reasonable cause for failure to pay the taxes due. This, of course, would mean that the failure was not willful, which is the verdict the jury returned. Consequently, since there is evidence which supports the verdict, it cannot be disturbed.

WAS THE INSTRUCTION ON THE MEANING OF THE TERM "WILLFUL" ERRONEOUS?

The following instructions on the meaning of "willful" were requested by the Government and refused:

> "An act is willful if it is voluntary, conscious, and intentional. If you find that plaintiff and/or third-party defendant knowingly used available funds to prefer other creditors over the United States then you must find that he acted willfully.
>
> "The Court instructs you that when a corporation meets its payroll it is presumed to have withheld therefrom the amount of taxes which the law requires it to withhold. The payment of wages to employees charges responsible persons with having in their hands the withholding taxes which is held as a trust fund. If a responsible person uses those funds for purposes other than payment of taxes, he or she is deemed to have acted willfully.
>
> "The Court further instructs you that if a responsible person pays employees their net wages at a time when the corporation does not have sufficient funds to pay the taxes withheld, and when the funds become available, he or she uses them to pay other creditors, that person acts willfully.
>
> "With regard to the phrase 'reasonable cause,' you are instructed that if you find that John and Robert Monday knew the taxes were owing, that there was money available to pay the taxes, and that John and Robert Monday paid other creditors instead of paying the taxes, then their failure to pay over the taxes was not due to reasonable cause."

The court gave the jury the following instructions as to the meaning of the word "willful" as used in § 6672 of the Internal Revenue Code of 1954:

> "You are instructed that for the plaintiff's and/or third-party defendant's failure to pay over the taxes

withheld to have been willful it is not necessary that there have been present any intent to defraud or to deprive the United States of taxes, nor is it necessary that bad motives or wicked design be shown.

"The term 'willful' means a voluntary, conscious and intentional act, done without reasonable cause, to prefer other creditors of the corporation over the government.

"Mere negligence, that is, failure to exercise ordinary care, in respect to collecting, truthfully accounting for or paying over the taxes is not enough to establish willfulness.

"A 'willful' act may also be described as one done intentionally, knowingly, and purposely, without justifiable excuse, as distinguished from an act done carelessly, thoughtlessly, heedlessly, or inadvertently.

"A 'willful' act differs essentially from a 'negligent' act. The former, that is 'willful,' is positive; and the latter, that is 'negligence,' is negative."

The Government contends that giving this instruction and denying the Government's requests was error and that a new trial is therefore required.

To support its definition of "willful," the Government relies on *Bloom* v. *United States*, 272 F.2d 215 (9th Cir. 1959). *Bloom* involved a taxpayer suit for refund under the earlier version of the provisions of the Internal Revenue Code now before this court. The Government had assessed a penalty against Bloom as a responsible officer in order to recover social security and withholding taxes which were withheld from employee wages but never paid to the Government.

The court in *Bloom* held that it was not proper to include criminal intent in the definition of "willful." The court was unable to agree with the following definition, asserted by Bloom:

> "'Thus, the basic elements of willfulness are evil motive, lack of justification, bad purpose, or something done or not done without justifiable excuse.' * * *" *Bloom* v. *United States*, *supra*, at 223-224.

That court did, however, adopt a definition of "willful" when it said:

> "* * * The decision of appellant as the responsible officer of the corporation not to have the corporation pay over to the government the withheld taxes was a voluntary, conscious, and intentional act to prefer other creditors of the corporation over the United States. In our view such conduct was willful within the meaning of [the statute]. * * *" *Bloom* v. *United States*, *supra*, at 223.

The same circuit, however, in *Gray Line Co.* v. *Granquist*, 237 F.2d 390 (9th Cir. 1956), held that reliance on the advice of an attorney and an Internal Revenue opinion was reasonable cause for failing to pay a disputed tax. There is no indication in *Bloom*, supra, that the court intended to overrule its holding in *Gray Line*, supra.

Gray Line, supra, involved the predecessor section of the Internal Revenue Act, 26 U.S.C. § 1718 (1952), which is essentially the same as § 6672 in the current Code. The plaintiff corporation sued for refund of a 100 per cent penalty which had been paid under protest. The penalty had been assessed for the transportation tax plaintiff should have collected from its passengers.

Plaintiff had not collected the tax in reliance on the opinion of an attorney and an opinion of the Special Deputy Tax Collector. The court held that this reliance

was in good faith and gave plaintiff reasonable cause to contest the liability for the tax even though a demand letter from Internal Revenue had been received subsequent to the advice of the collector. Consequently, the court concluded that plaintiff did not act willfully in failing to collect and pay the tax.

The fact situation before this court is far more analogous to that presented in *Gray Line*, supra, than it is to the facts of *Bloom*, supra. The evidence is that the Mondays were acting in good faith at all times. The Mondays relied on the specific permission of an officer of the Internal Revenue to continue in business as they did. In the view of this court, this certainly constitutes reasonable cause for failing to pay the taxes in question.

Other courts have taken positions compatible with that of *Gray Line*, supra. In *Frazier* v. *United States*, 304 F.2d 528 (5th Cir. 1962), the court held that failure to pay the taxes involved was willful and without reasonable cause when (1) net wages were paid to employees although the corporation did not have sufficient funds to pay the taxes withheld, and (2) when the funds became available to pay the taxes, the Government was not paid. The court agreed that "without reasonable cause" is a part of the test for "willful" failure, but concluded that there was no reasonable cause presented here as a matter of law.

A district court adopted a similar view to that expressed in *Gray Line*, supra, in *Cross* v. *United States*, 204 F. Supp. 644 (E.D. Va. 1962). The court held in *Cross* that there was no "willful" failure to pay the transportation taxes in question because the plaintiff acted in reliance on the advice of two attorneys. When one of the attorneys got an opinion from the Internal Revenue Service that was not favorable, Cross paid the taxes under protest and

sued for refund. Under the facts in *Cross*, supra, the district court concluded that the original failure to pay the taxes was not "willful" within the meaning of § 6672 of the Internal Revenue Code.

The situation in which the Mondays found themselves presents even more compelling reasons for concluding that the failure to pay the taxes was not "willful." The Mondays continued their business and paid for supplies in reliance upon the specific permission of an officer of the Internal Revenue rather than mere advice of attorneys.

The only Seventh Circuit case brought to the attention of this court is *Flan* v. *United States*, 326 F.2d 356 (7th Cir. 1964). This was an action for refund of the penalty exacted for failure to pay withholding and F.I.C.A. taxes withheld from wages. Flan was the president and principal stockholder of the corporation and the only active officer. He signed and filed all returns in question, and in some instances enclosed partial payment on the taxes due. It was found as a fact that there were sufficient funds in the corporation's bank accounts at all times in question to pay the delinquent taxes in issue.

The *Flan* case was tried to the court. The court found as facts that Flan had ultimate authority to determine who the corporation would pay and that the corporation bank accounts had, at all times, sufficient funds to pay the delinquent taxes involved. The trial court held that "willfully" as used in § 6672 meant only "knowingly," "voluntarily," or "intentionally," and held that Flan was liable for the penalty assessed. The court of appeals affirmed.

On appeal, Flan argued that "willful failure to account" requires that the failure be "without reasonable cause." The court of appeals concluded, however, that the fact situation presented made "reasonable cause" inapplicable

to the definition of "willful." In the view of this court, such action by the court of appeals does not constitute a rejection of the use of "reasonable cause" in the definition of "willful" when in fact reasonable cause does exist.

The facts in the case at bar are distinguishable from those presented in *Flan*. The Mondays had specific permission from the Internal Revenue to continue operations as they did; Flan asserted no such permission or any other fact which could constitute reasonable cause. This distinction makes it a question for the jury to determine whether the failure of the Mondays to pay the taxes in question was with reasonable cause and therefore not willful.

WAS EVIDENCE OF THE CORPORATION'S FINANCIAL CONDITION AND BANKRUPTCY ERRONEOUSLY RECEIVED?

During the course of the trial, evidence relating to the financial condition of the corporation during the times in question and the bankruptcy proceedings of the corporation was received over the objection of the Government.

The Government contends that such evidence prejudiced its case and was irrelevant.

Evidence dealing with the financial condition of the corporation and with the ensuing bankruptcy is clearly relevant to the understanding by the jury of whether or not the officers were acting in good faith and had reasonable cause not to pay the taxes in question. The jury should have the whole picture of the financial operation of the corporation as it relates to its ability to pay.

WAS TESTIMONY IMPROPERLY ADMITTED AS EXPERT OPINION?

During the trial, a deposition taken of Deane Nichol, a certified public accountant, was introduced as evidence over the objection of the Government. Mr. Nichol was in New York undergoing surgery at the time of the trial, and the deposition had been taken in the presence of counsel for all parties with the knowledge that he would be unavailable for trial.

Mr. Nichol was the accountant employed by the P. T. Monday Tea Company to audit the corporation's books and prepare financial statements from about October 1960 to about March 1961. During the taking of the deposition, it was agreed that the deposition was to be both for discovery and for use at trial. Numerous objections of various natures were made by counsel for all parties during the taking of the deposition, but no questions were certified to the court.

At the trial, the Government objected to the qualification of Mr. Nichol as an expert for the purposes of this trial.

Since this court has already ruled on the relevance of the financial condition of the corporation at the times in question, it will not be repeated at this point. Suffice it to say that since the financial condition of the corporation was relevant to the question of the Monday brothers acting in good faith and with reasonable cause, expert evidence on the financial condition was proper.

Jones on Evidence, Vol. 4, §§ 413, 414, 420, 437 (1958) and 1968 Supplement, and authority cited therein, clearly indicates that Mr. Nichol was properly qualified as an expert and his testimony was properly admitted. In view of his qualification as an expert, the instruction dealing with expert testimony was also in order.

WAS IT ERROR NOT TO INSTRUCT THAT THE PENALTY IMPOSED BY THE STATUTE IS NOT A PENALTY?

The court gave the following instructions with regard to the penalty assessed against the Mondays under § 6672:

> "The sums involved in this suit arise from the claimed liability of the P. C. Monday Tea Company to pay over income taxes and social security taxes which were withheld from the wages of its employees but which were not paid over to the government.
>
> "The money sought by the United States against Robert Monday and/or John Monday in this action was not assessed against each of them as a tax owing by him but as a penalty for an alleged violation of the law. The penalty is not imposed as a remedial provision designed simply to enable the government to collect the taxes due. The liability asserted against Robert Monday and/or John Monday is wholly distinct from and in addition to, not a substitute for, the corporation's liability for the withheld taxes.
>
> "The purpose of the statute is not to punish but to secure the collection of a fund that has passed into the hands of the employer from the employees, which is a special trust fund, the employer acting as a collecting agency for the United States. If a corporation meets its payroll, it is presumed that it received and had in its possession and under the control of its officers the withholding taxes."

The Government contends that it was error to use the word "penalty" in the instructions, although that is the very word used in the statutes. This court believes it was necessary to instruct the jury as it did. Had the provision been intended by Congress to be something other than a penalty, another word could certainly have been used. Again, this court respectfully declines to amend a congressional act.

For all the foregoing reasons,

IT IS THEREFORE ORDERED that the motion of the United States of America for judgment notwithstanding the verdict be and it is hereby denied.

IT IS FURTHER ORDERED that the motion of the United States of America for a new trial likewise be and it is hereby denied.

Dated at Milwaukee, Wisconsin, this 14th day of January, 1969.

John W. Reynolds
U. S. District Judge

APPENDIX C

JUDGMENT OF THE COURT OF APPEALS FOR THE SEVENTH CIRCUIT

Thursday, January 29, 1970

Before

Hon. Win G. Knoch, Senior Circuit Judge

Hon. Walter J. Cummings, Circuit Judge

Hon. William E. Steckler, District Judge

(Caption Omitted)

This cause came on to be heard on the transcript of the record from the United States District Court for the Eastern District of Wisconsin, and was argued by counsel.

On consideration whereof, it is ordered and adjudged by this court that the judgment of the said District Court in this cause appealed from be, and the same is hereby, REVERSED, with costs, and that this cause be, and it is hereby, REMANDED to the said District Court with instructions to enter judgment for the United States against John A. Monday and to grant a new trial to Robert Monday to determine, upon proper instructions to the jury, the question of his willfulness, in accordance with the opinion of this Court filed this day.

In the Supreme Court of the United States

OCTOBER TERM, 1969

No. 1623

ROBERT W. MONDAY AND JOHN A. MONDAY, PETITIONERS

v.

UNITED STATES OF AMERICA

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

BRIEF FOR THE UNITED STATES IN OPPOSITION

OPINIONS BELOW

The opinion of the district court (Pet. App. 15–28) is reported at 294 F. Supp. 1384. The opinion of the court of appeals (Pet. App. 1–14) is reported at 421 F. 2d 1210.

JURISDICTION

The judgment of the court of appeals was entered on January 29, 1970 (Pet. App. 29). Petitioner's petition for rehearing was denied on March 17, 1970. The petition for a writ of certiorari was filed on May 28, 1970. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

QUESTIONS PRESENTED

1. Whether a corporate officer, who knowingly, voluntarily and intentionally fails to pay over withheld taxes to the government in violation of his duty to do so, may escape the personal liability for such taxes imposed by Section 6672 of the Internal Revenue Code by showing "reasonable cause" for his failure.

2. Whether the court of appeals, in reversing the judgment of the district court with instructions to enter judgment for the United States against petitioner John A. Monday, violated his constitutional right to trial by jury and deprived him of property without due process of law.

STATUTES INVOLVED

The pertinent provisions of Sections 3102, 3402, 6671, 6672 and 7501 of the Internal Revenue Code of 1954 are set forth in the Appendix, *infra*, pp. 11–12.

STATEMENT

During the third and fourth quarters of 1960, the P. C. Monday Tea Company, of which petitioners were the officers responsible for the collection and payment to the government of federal income and social security taxes, paid wages to its officers and employees and withheld such taxes therefrom. It failed, however, to pay these withheld funds (totaling more than $12,000) to the government on October 31, 1960, and on January 31, 1961, the respective due dates for quarterly payments. Instead, the company, which was in a perilous financial condition, used the funds to pay business creditors for antecedent debts and for merchandise

purchased C.O.D. (Pet. App. 1–2; R. 201, 268, 289, 426–427.)[1] Consequently, the Internal Revenue Service determined that petitioners were liable for the 100 percent penalty imposed by Section 6672 of the Internal Revenue Code on responsible corporate officers who "willfully" fail to pay over withheld taxes (Pet. App. 3–4).

At trial before a jury, petitioner John Monday testified that during the period in issue he was aware that the withheld taxes were due and owing to the government and that he used such funds to pay business creditors of the company (Pet. App. 10; R. 428). Petitioner Robert Monday claimed that he was unaware of the withholding tax deficiency and therefore did not act "willfully" under the statute (R. 207, 242). There was testimony at trial, however, contradicting this assertion (Pet. App. 10–11; R. 219–220, 268, 277–278, 371, 388, 431).

Petitioners sought to justify their intentional and knowing misappropriation of government funds by reference to several meetings which they had with an Agent Pietrzak of the Internal Revenue Service. The first meeting took place on November 30, 1960, which was one month after the due date for third-quarter taxes. The P. C. Monday Tea Company had already misappropriated the tax monies collected from its employees during the third quarter of 1960, and thus, when this meeting took place, had created a deficiency situation which left the government the alternatives of put-

[1] "R." references are to the separately bound two-volume Appendix to petitioner's brief in the court of appeals.

ting the company out of business or permitting it to use current funds under strict limitations. According to petitioners, they were told by Mr. Pietrzak that if they kept current in their tax payments from then on, they would be permitted to continue operations and to pay for their merchandise on a C.O.D. basis. (Pet. App. 11–12; R. 432, 438–439.)

The second meeting was held in the latter part of March, 1961, after the P. C. Monday Tea Company, in derogation of the promise to Mr. Pietrzak that it would keep current, and in violation of the statute, had appropriated tax monies collected during the fourth quarter of 1960 to pay business creditors. At this meeting, Mr. Pietrzak required the company to pay $4,500 to cover taxes for the first quarter of 1961. (Pet. App. 12; R. 279, 433–434.)

After the jury was instructed, over the government's objection, that the term "willful" as used in Section 6672 "means a voluntary, conscious and intentional act, *done without reasonable cause*" (emphasis added) (Pet. App. 21), a verdict was returned which found that neither petitioner had acted willfully in failing to pay over the withheld taxes on the respective due dates (Pet. App. 4). The court of appeals ruled that reasonable cause was not a relevant consideration in determining willfullness. It reversed the judgment of the district court, which had been entered in accordance with the verdict, with instructions to enter judgment for the United States against petitioner John A. Monday and to grant a new trial to petitioner Robert Monday before a jury properly instructed on the issue of willfulness (Pet. App. 29).

ARGUMENT

The decision below is correct. There is no direct conflict or other warrant for further review.

1. Despite its denomination as a "penalty" assessment, it is well settled that the statutory liability imposed by Section 6672 of the Code is essentially civil in nature. *Cash* v. *Campbell*, 346 F. 2d 670, 673 (C.A. 5); *Botta* v. *Scanlon*, 314 F. 2d 392 (C.A. 2); *United States* v. *Strebler*, 313 F. 2d 402 (C.A. 8); *Bloom* v. *United States*, 272 F. 2d 215 (C.A. 9), certiorari denied, 363 U.S. 803.[2] Its primary purpose is to prevent the unnecessary loss of withheld federal income and social security tax monies, which, under Section 7501 (a), constitute a special fund in trust for the United States, by permitting the tax authority to reach those responsible for the misappropriation of such monies. *United States* v. *Graham*, 309 F. 2d 210, 212 (C.A. 9); *White* v. *United States*, 372 F. 2d 513, 516 (Ct. Cl.).

Thus, as petitioners concede (Pet. 13), the liability imposed by Section 6672 is not dependent upon a finding of evil motive or specific intent to defraud the government or deprive it of revenue on the part of the corporate officers. *White* v. *United States*, *supra*, p. 521. A responsible officer has acted "willfully" under the statute if he voluntarily, consciously and intentionally—as opposed to accidentally—elects to use the withheld funds in an impermissible manner (*e.g.*, to pay

[2] Section 7201 of the Code, on the other hand, imposes a criminal penalty for willful failure to collect or pay over taxes. See, *e.g.*, *Wilson* v. *United States*, 250 F. 2d 312 (C.A. 9).

corporate debts). *Spivak* v. *United States*, 370 F. 2d 612, 615 (C.A. 2), certiorari denied, 387 U.S. 908; *Cross* v. *United States*, 311 F. 2d 90, 94 (C.A. 4); *Hewitt* v. *United States*, 377 F. 2d 921, 924 (C.A. 5); *Flan* v. *United States*, 326 F. 2d 356, 358 (C.A. 7); *Bloom* v. *United States*, *supra*, p. 223; *Scott* v. *United States*, 354 F. 2d 292, 295 (Ct. Cl.). In line with these decisions, the court of appeals correctly concluded that "reasonable cause" and "justifiable excuse" are not proper considerations in determining whether a responsible officer willfully used withheld funds to pay corporate creditors.[3]

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[3] What petitioners allege as reasonable cause for their willful failure to pay over the tax monies—that their conduct was expressly authorized by a responsible Internal Revenue Service officer—is not even supported by the record. As the court of appeals noted (Pet. App. 11–12), the first meeting with Agent Pietrzak took place after petitioners had already misappropriated taxes withheld for the third quarter of 1960, and thus could provide no excuse for this action. Neither at this meeting nor at the subsequent meeting in March 1961, did the agent give the officers permission to deplete further the assets of the company available to satisfy the government's claim; nor did he advise them that, by permitting the business to remain in operation, he was relieving them of their potential liability under Section 6672 for any further withholding tax deficiencies that might arise. Moreover, at the first meeting, Agent Pietrzak specifically instructed the company to keep current (R. 279, 432), thereby precluding any claim that its subsequent failure to remit the fourth quarter taxes resulted from reliance upon his authorization to continue their business. The court of appeals therefore correctly concluded (Pet. App. 12) that, in any event, petitioners "failed to disclose any action by the Government upon which they could reasonably have relied as the grounds for their failure to collect and remit any of the taxes withheld from their employees."

2. The conflict which petitioners contend (Pet. 9–10) exists between the decision below and that of the Fifth Circuit in *Frazier* v. *United States*, 304 F. 2d 528, is not a real one. Although the court in *Frazier* did include the term "reasonable cause" in its definition of "willfulness" under Section 6672, the outcome of that case was not in any way dependent upon that construction of the statute. As the court itself there noted (304 F. 2d at 530):

> For the present we need only hold that in a civil case where a responsible officer paid employees their net wages at a time when the corporation had insufficient funds to cover the taxes thereon and, when such funds became available, preferred subsequent creditors over the United States, knowing at all times his obligation to pay such taxes, his failure to pay was "without reasonable cause" and "willful" within the meaning of Section 6672.

The Fifth Circuit's inclusion of the phrase "without reasonable cause" thus was irrelevant to its holding on the facts presented in *Frazier*. That holding on the facts does not conflict with the decision below.

Similarly, although in both *Cash* v. *Campbell*, 346 F. 2d 670, 672 (C.A. 5), and *Gefen* v. *United States*, 400 F. 2d 476 (C.A. 5), the Fifth Circuit mentioned "reasonable cause" as part of the "willfulness" test, its holdings on the facts of those cases in no way rested on the presence or absence of that factor, and the comments were in the nature of dicta. Whether, if confronted with the actual issue, the Fifth Circuit would permit a taxpayer to invoke "reasonable cause" where

the Seventh Circuit would not, remains to be determined. The allegation of conflict at this point is premature.[4]

3. Petitioner John Monday's claim that his constitutional rights to trial by jury and due process were denied by the court of appeals when it reversed the jury verdict in his favor and directed the district court to enter judgment against him is without merit. This Court has stated that "When the evidence is such that without weighing the credibility of the witnesses there can be but one reasonable conclusion as to the verdict, the court should determine the proceeding * * * without submission to the jury * * *." *Brady* v. *Southern Ry. Co.*, 320 U.S. 476, 479-480. And such

[4] There is no merit to petitioners' contention (Pet. 9-10) that several other circuit court cases conflict with the decision in the present case. *Gray Line Co.* v. *Granquist*, 237 F. 2d 390 (C.A. 9), involves a situation where the responsible officer was advised by counsel that the corporation had no obligation to collect the particular tax for the government. Hence, it did not involve the prerequisite of willfulness that the officer be aware that the tax was due and owing to the government. The decision did not rest upon a showing of reasonable cause for a willful failure to pay over funds collected for the government *and known to be due it*. Indeed, if *Gray Line* were to be construed as holding that reasonable cause can excuse an otherwise willful failure to pay over taxes known to be due and owing, it would then follow that it was overruled by the Ninth Circuit's later decision in *Bloom* v. *United States*, *supra*, where that proposition was squarely rejected.

In *United States* v. *Stygler*, 313 F. 2d 702 (C.A. 8), the question of willfulness was not even at issue. In *United States* v. *Slattery*, 333 F. 2d 844 (C.A. 3), the district court's judgment was affirmed *per curiam* without any reference to which, if any, of the alternative grounds given by the district court to support its decision were relied upon by the court of appeals.

action (which, indeed, is authorized by Rule 50 of the Federal Rules of Civil Procedure) has been repeatedly upheld by this Court against assertions that it violates the Seventh Amendment. See, *e.g.*, *Calloway* v. *United States*, 319 U.S. 372, 389. None of the cases cited by petitioners (Pet. 14) purport to hold to the contrary.

Since petitioner John Monday's only defense against the application of the penalty was based upon the alleged "reasonable cause" for his concededly willful act, the court below, having ruled as a matter of law that this was not a permissible consideration, properly directed that judgment be entered against him.

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted.

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JUNE 1970.

APPENDIX

Internal Revenue Code of 1954 (26 U.S.C. (1958 ed.)):

SEC. 3102. DEDUCTION OF TAX FROM WAGES.

(a) *Requirement.*—The tax imposed by section 3101 shall be collected by the employer of the taxpayer, by deducting the amount of the tax from the wages as and when paid. * * *

* * * * * *

SEC. 3402. INCOME TAX COLLECTED AT SOURCE.

(a) *Requirement of withholding.*—Every employer making payment of wages shall deduct and withhold upon such wages * * * a tax equal to 18 percent of the amount by which the wages exceed the number of withholding exemptions claimed, multiplied by the amount of one such exemption as shown in subsection (b)(1).

* * * * * *

SEC. 6671. RULES FOR APPLICATION OF ASSESSABLE PENALTIES.

(a) *Penalty assessed as tax.*—The penalties and liabilities provided by this subchapter shall be paid upon notice and demand by the Secretary or his delegate, and shall be assessed and collected in the same manner as taxes. Except as otherwise provided, any reference in this title to "tax" imposed by this title shall be deemed also to refer to the penalties and liabilities provided by this subchapter.

(b) *Person defined.*—The term "person," as used in this subchapter, includes an officer or employee of a corporation, or a member or employee of a partnership, who as such officer, employee, or member is under a duty to perform the act in respect of which the violation occurs.

SEC. 6672. FAILURE TO COLLECT AND PAY OVER TAX, OR ATTEMPT TO EVADE OR DEFEAT TAX.

Any person required to collect, truthfully account for, and pay over any tax imposed by this title who willfully fails to collect such tax, or truthfully account for and pay over such tax, or willfully attempts in any manner to evade or defeat any such tax or the payment thereof, shall, in addition to other penalties provided by law, be liable to a penalty equal to the total amount of the tax evaded, or not collected, or not accounted for and paid over. No penalty shall be imposed under section 6653 for any offense to which this section is applicable.

SEC. 7501. LIABILITY FOR TAXES WITHHELD OR COLLECTED.

(a) *General rule.*—Whenever any person is required to collect or withhold any internal revenue tax from any other person and to pay over such tax to the United States, the amount of tax so collected or withheld shall be held to be a special fund in trust for the United States. The amount of such fund shall be assessed, collected, and paid in the same manner and subject to the same provisions and limitations (including penalties) as are applicable with respect to the taxes from which such fund arose.

* * * * * * *

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